**Cerner Corp**

 CERN

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**Cerner should benefit greatly from the increasing spending on healthcare infrastructure.**



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**Analyst Note**

[Revenue Issues Continue for Cerner; Lowering Our Fair Value Estimate, but Shares Still Undervalued](http://quicktake.morningstar.com/StockNet/san.aspx?id=742002)   
by Vishnu Lekraj, 02/17/2016

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**Analyst Note** 02/17/2016

While Cerner met our expectations for its fourth quarter, we are lowering our fair value estimate to $63 per share from $69. Cerner’s management team once again missed its own revenue guidance, and we believe the firm is experiencing increasing pressure within its operating environment. Considering these latest developments, we now believe top-line growth will moderate slightly faster than we initially expected. Additionally, we believe competition from current and new healthcare IT players has accelerated given the growing need of providers to build in new reimbursement infrastructure and the prime opportunity this presents to the entire HCIT market. As a result, we believe Cerner will experience greater sales and research and development expenses over the medium term than we initially expected. These modeling adjustments lead to a reduction in our explicit forecast revenue growth and operating margin expansion assumptions. However, the firm’s stock trades below our reduced fair vale estimate and presents investors an opportunity to acquire shares of a solid healthcare firm at a material discount.

**Investment Thesis** 08/06/2015

The outlook for the healthcare IT sector is solid, with the combination of Affordable Care Act regulation and changing reimbursement structures motivating providers (hospitals, physician offices, diagnostic centers, and integrated provider networks) to either revamp or build new IT infrastructure. With a highly trusted brand, leading software products, and high customer switching costs, we believe Cerner has a wide economic moat. The integrated and essential nature of the firm’s offerings makes it a key player within the healthcare IT market and will allow it to produce economic profits over a significant period.   
  
Strong customer switching costs is the bedrock of Cerner’s major competitive advantages. Long product implementation periods (18-24 months), highly integrated/customized software packages, and service contracts that last years lock major provider clients into the firm’s grasp. Boosting the long-term demand for Cerner’s services are several factors including the increasing complexity of Medicare reporting, strong growth of value-based payer reimbursement schemes, and electronic medical records regulatory compliance. The combination of these factors solidifies the firm’s long-term economic profitability.   
  
What differentiates Cerner from its competitors is a strategy of developing and building its product portfolio in-house. Many large healthcare IT servicers have acquired varying software manufacturers, which creates less continuity within their product lineups. This dynamic can give Cerner an material advantage when competing for new business as its products are relatively more integrated and seamless.   
  
While the need for EMR services will be a pillar for future industry growth, we believe predictive analytics and patient population management will also play major roles in driving healthcare IT demand as providers are increasingly required to produce more value for their services. As a leader in developing analytical products, Cerner is well positioned to benefit from this secular growth trend.

### orningstar's Take

## CERN

* [Analyst](javascript:chgTab('analyst');)

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| --- | --- | --- | --- |
| Price 04-21-2016 | | Fair Value Estimate | Uncertainty |
| 58.46 USD | | 63 USD | Medium |
|  | | | |
| Consider Buy | | Consider Sell | Economic Moat |
| 44.1 USD | | 85.05 USD | Wide |
|  | | | |
| Stewardship Rating | | | |
| Standard | | | |
|  | | | |
|  |  | | | |
| Bulls Say | | | | |
|  | | | | |
| • | Cerner is a tier-one player in the healthcare IT industry as its software is highly integrated into the operations of several large provider networks. | | | |
|  | | | | |
| • | The firm has internally developed much of its software, which makes its product lineup one of the most seamless and effective within the healthcare IT sector. | | | |
|  | | | | |
| • | The secular demand tailwinds for Cerner’s products are robust given ACA mandates that require providers to upgrade their health records management systems. This highly positive trend will be enhanced over the next several years by changing payer reimbursement structures. | | | |
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| Bears Say | |
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| • | Given the critical nature of Cerner’s products, any issue with its software development can create major operational headwinds. |
|  | |
| • | Competition could increase as many well capitalized players have made major moves into the healthcare IT market. |
|  | |
| • | A material portion of Cerner’s products have been developed to assist providers with regulatory compliance and any governmental changes to current mandates would create headwinds for the firm. |
|  | |

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| --- | --- | --- | --- | --- |
| **Name** | **Price** | **% Chg** |  | **TTM Sales  $ mil** |
|  | | | | |
| Cerner Corp | $58.46 | 0.17 |  | 4,425 |
| [IMS Health Holdings Inc](http://quotes.morningstar.com/stock/IMS/s?t=0P00012IIY&culture=en-US) | $26.86 | -0.70 |  | 2,921 |
| [athenahealth Inc](http://quotes.morningstar.com/stock/ATHN/s?t=0P00009PDK&culture=en-US) | $134.16 | -2.58 |  | 925 |
| [WebMD Health Corp](http://quotes.morningstar.com/stock/WBMD/s?t=0P000005VS&culture=en-US) | $61.65 | -0.80 |  | 636 |
| [Inovalon Holdings Inc](http://quotes.morningstar.com/stock/INOV/s?t=0P00015BGX&culture=en-US) | $18.23 | -4.35 |  | 437 |
| [Veeva Systems Inc Class A](http://quotes.morningstar.com/stock/VEEV/s?t=0P0000ZOOL&culture=en-US) | $26.66 | 2.34 |  | 409 |

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